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IN THE

Supreme Court of the United States

October Term, 1959.

No. 289

BAUSCH & LOMB OPTICAL COMPANY,

Petitioner

—v.—

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The petitioner prays that a writ of certiorari be issued to review the judgment of the United States Court of Appeals for the Second Circuit (R., p. 59, and Appendix A hereto), affirming the decision of the Tax Court of the United States (R., p. 47).

Opinions Below

The opinion of the Tax Court (R., p. 41) is reported at 30 T. C. 602. The opinion of the Court of Appeals (R., p. 53, and Appendix B hereto) is not yet reported.

Grounds for Invoking Jurisdiction of the Court

The judgment of the Court of Appeals was dated and entered May 19, 1959 (R., p. 60, and Appendix A hereto). Jurisdiction to issue the writ prayed for is vested in this

Court by Section 1254 of Title 28 of the United States Code.

Question Presented

Does the prior ownership by one corporation of stock in another corporation, substantially all the properties of which are acquired by the first corporation in exchange solely for its voting stock, followed by the liquidation of the second corporation, all pursuant to a plan of reorganization, prevent nonrecognition of gain or loss from the reorganization?

Judge Harron of the Tax Court held that it did, and the Court of Appeals affirmed her decision.

Statutes Involved

The statutes involved are Sections 112(b)(3) and (4) and (g) of the Internal Revenue Code of 1939, to which Sections 354(a)(1) and (2), 361(a), and 368(a)(1) and (b), of the Revenue Code of 1954, are similar.

Section 112(g) of the 1939 Code (U. S. C., Title 26), as in force in 1950, provides the following definition of "reorganization":

> "(1) The term 'reorganization' means (A) a statutory merger or consolidation, or (B) the acquisition by one corporation, in exchange solely for all or a part of its voting stock, of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation, or (C) the acquisition by one corporation, in exchange solely for all or a part of its voting stock, of substantially all the properties of another corporation, but in determining whether the

exchange is solely for voting stock the assumption by the acquiring corporation of a liability of the other, or the fact that property acquired is subject to a liability, shall be disregarded, or (D) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its shareholders or both are in control of the corporation to which the assets are transferred, or (E) a recapitalization, or (F) a mere change in identity, form, or place of organization, however effected.

(2) The term 'a party to a reorganization' includes a corporation resulting from a reorganization and includes both corporations in the case of a reorganization resulting from the acquisition by one corporation of stock or properties of another."

Section 112(b)(3) of the 1939 Code provides:

"(3) STOCK FOR STOCK ON REORGANIZATION.—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization."

Section 112(b)(4) of the 1939 Code provides:

"(4) SAME—GAIN OF CORPORATION.—No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization."

Statement of the Case

The petitioner for over a century has been engaged in the manufacture and sale of ophthalmic products (R., p.

11). Until shortly prior to 1950 the petitioner's commercial ophthalmic products were largely distributed through five subsidiary corporations, including Riggs Optical Company Consolidated, of Chicago, Illinois, a Delaware corporation (herein called "Riggs"), which was incorporated in 1922. The petitioner controlled these subsidiaries through the ownership of a majority of the stock of each. In the late 1940's, as one aspect of the petitioner's post-war effort to regain the commercial business which it had lost during its preoccupation with making military equipment, it adopted a program of merging the separate subsidiaries in order to effect economies which were made possible thereby. The officers and directors of the petitioner and also the individual minority stockholders of the subsidiaries, most of whom were active in the distribution operations, felt that it would be preferable to effect the mergers in such a way that the minority stockholders would emerge as stockholders of the petitioner rather than remain stockholders of separate subsidiaries. Pursuant to this program the subsidiaries were successively merged into the petitioner, the first three before and the fifth after Riggs (R., pp. 3, 11, 12, 20, 21).

Negotiations for the merger of the petitioner and Riggs were initiated in the fall of 1949. Early in 1950, as a step in the program of merger, a reorganization plan in the form of a letter to Riggs dated March 1, 1950, was prepared after conferences between the directors of the two companies (R., pp. 5-10). As approved by the boards of directors of both companies, with the elimination of the parenthetical clause beginning in the middle of line 5 of subparagraph (a) of paragraph 3, the plan provided for the petitioner issuing 105,941 of its voting common shares in exchange for the conveyance of all of the properties of Riggs to the petitioner. It also provided that thereafter the stock of the petitioner received for the Riggs properties

be distributed to the Riggs stockholders and that Riggs be dissolved (R., pp. 12-17).

On April 21, 1950, pursuant to the plan, the petitioner issued 105,508 shares of the petitioner's authorized but previously unissued common stock to Riggs (plus 433 shares to Riggs employees who had become entitled thereto), paying the federal issue tax thereon, and took delivery of an instrument of conveyance of all the assets of Riggs, dated April 13, 1950, expressed to be effective at the close of business April 22, 1950 (R., pp. 17, 18).

On May 2, 1950, the stockholders of Riggs voted unanimously in favor of dissolution of the corporation. Thereupon a certificate of dissolution was filed with the Secretary of State of Delaware and the 105,508 shares of common stock of the petitioner were distributed to the Riggs stockholders in exchange for their stock, the petitioner receiving 84,347 shares. The stock transfer taxes imposed by the United States and by the State of New York were paid in respect of all such 105,508 shares. The shares of its common stock received in distribution from Riggs were held by the petitioner in its treasury, and portions of such shares were sold by the petitioner to its employees in 1954, 1955 and 1956 (R., pp. 4, 5, 19, 20).

Upon a re-audit of the petitioner's federal income tax return for 1950 the Commissioner took the position that the petitioner had not acquired substantially all of the assets of Riggs solely for voting stock, and charged the petitioner with tax on the theory that it received taxable gain on the distribution to it of shares of its own stock in exchange for its shares of stock in Riggs. The petitioner duly filed an appeal to the Tax Court of the United States, as authorized by Section 272 of the Internal Revenue Code of 1939 and Section 6213 of the Internal Revenue Code of 1954 (R., p. 1).

Reasons Relied on for Allowance of Writ

It is submitted that in holding that the transaction of acquisition of the Riggs assets for voting stock, followed by the liquidation of Riggs, did not constitute a non-taxable reorganization because on the liquidation of Riggs the petitioner in exchange for its stock in Riggs received some of its own stock which it thereafter held as treasury stock, the Court of Appeals erred.

Thereby the Court of Appeals has decided an important question of federal law, which has not been, but should be, settled by this Court; has decided a federal question in a way in conflict with fundamental principles applied in decisions of this Court; and has rendered a decision in conflict with the decision of another Court of Appeals in a similar matter.

Bona fide corporate reorganizations have been accorded special treatment in the revenue acts beginning in 1918, at first rather sketchily, but later with more particularity.* In the early period, because of attempts to treat as non-taxable reorganizations transactions which were actually sales, the courts laid down the requirements of continuity of interest and business purpose, which have since been uniformly applied. The initial leading cases were *Pinellas Ice & Cold Storage Co.* v. *Commissioner*, 21 B. T. A. 425, aff. 57 F. (2d) 188, aff. 287 U. S. 462, and *Cortland Specialty Co.* v. *Commissioner*, 22 B. T. A. 808, aff. 60 F. (2d)

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* See R. A. 1918, Sec. 202(b); R. A. 1921, Sec. 202(c)(2); R. A. 1924, Sec. 203(b)(2)(3), (h) and (i); R. A. 1926, Sec. 203(b)(2)(3), (h) and (i); R. A. 1928, Sec. 112(b)(3)(4), (i) and (j); R. A. 1932, Sec. 112(b)(3)(4), (i) and (j); R. A. 1934, Sec. 112(b)(3)(4), (g) and (h); R. A. 1936, Sec. 112(b)(3)(4), (g) and (h); R. A. 1938, Sec. 112(b)(3)(4), (g) and (h); I. R. Code of 1939, Sec. 112(b)(3)(4), (g) and (h); R. A. 1939, Sec. 213(b); I. R. Code of 1954, Secs. 354(a)(1)(2), 361(a) and 368(a)(1) and (b).

937 (C. C. A. 2), cert. denied 288 U. S. 599. As the attempts to exploit the reorganization provisions continued, Congress in 1934 amended the definition of reorganization to limit the consideration for stock or assets of the acquired corporation to voting stock of the acquiring corporation. That requirement was strictly met in the present case, and the statutory provisions were fully observed.

As stated above, the petitioner issued solely voting stock for all the assets of Riggs in pursuance of the admitted business purpose of continuing the activities of Riggs, not of terminating them as in the case of an ordinary liquidation. By the subsequent dissolution of Riggs its stockholders became stockholders of the petitioner, assuring a complete continuity of interest. Every underlying concept of a true reorganization was satisfied.

If the petitioner had previously held no stock in Riggs, and had proceeded precisely as it did, first acquiring the Riggs assets in exchange for voting stock and then procuring the dissolution of Riggs, the validity of the reorganization would not have been questioned. On the other hand, if the petitioner had held at least 80 per cent. of the Riggs stock and had merely caused the liquidation of Riggs, no tax liability would have been incurred, although the petitioner could not so clearly have succeeded to all the assets and business of Riggs (I. R. C. 1939, Section 112(b)(6)).

The effect of the decision of the lower courts is that a corporation holding no stock in another corporation may accomplish a tax-free reorganization by issuing solely voting stock for all the assets of the other corporation, which would then be dissolved; and a corporation holding 80 per cent. of the stock of another corporation may simply cause the liquidation of the other corporation and receive most or all of its assets in a tax-free liquidation; but a corporation already owning stock in another corporation, but less

than 80 per cent., may be (or as in this case will be) subject to tax if it issues voting stock for the assets of the other corporation, which then dissolves and distributes to its stockholders the stock received for its assets from the acquiring corporation.

That is a conclusion which is senseless and has no basis in the history and purpose of the statute or in its language. The requirement first introduced in the 1934 Act for the exchange solely of voting stock for the assets of another corporation was intended to assure the continuity of interest in the acquiring corporation of the stockholders of the acquired corporation, and here the previously existing ownership of stock in the acquired corporation by the acquiring corporation further insured such continuity of interest. No taint of a sale was present.

The 1934 House bill provided for the tax-free acquisition by one corporation of the properties of another only by a statutory merger or consolidation, but the Senate amended the bill by authorizing the tax-free acquisition of assets by the issue of voting stock. In the report of the Committee on Finance on the 1934 bill (1939-1 C. B. (Part 2) 598) it was stated:

> "Your committee is in complete agreement with the purposes of the House bill which aim at tax-avoidance schemes in this connection. However, some modifications are recommended in order to bring about a more uniform application of the provisions in all 48 of the States. Not all of the States have adopted statutes providing for mergers or consolidations; and, moreover, a corporation of one State cannot ordinarily merge with a corporation of another State. The committee believes that it is desirable to permit reorganizations in such cases, with restrictions designed to prevent tax avoidance. Consequently, the committee

recommends the insertion in the House bill of an addition to the definition of the term 'reorganization' as follows:

'(B) the acquisition by one corporation in exchange solely for its voting stock; of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation; or of substantially all the properties of another corporation;'

The committee believes that these transactions, when carried out as prescribed in this amendment, are in themselves sufficiently similar to mergers and consolidations as to be entitled to similar treatment."

The Court of Appeals' opinion expresses no view as to the effect of an acquiring corporation previously holding a small interest in the acquired corporation, although treating the petitioner's large interest as fatal to a non-taxable reorganization (App. B, p. 26). Accordingly, a wide gap is left in the construction of the statute, which in the public interest should be filled. We venture to say that Judge Medina's opinion shows no conception of the fundamental principles of reorganizations under the tax law, as where he says (App. B, p. 26):

"We merely hold that the attempt to thwart taxation in this case by carrying out the liquidation process in two steps instead of one fell short of meeting the requirements of a 'C' reorganization. See *Gregory* v. *Helvering*, 1935, 293 U. S. 465; *Helvering* v. *Alabama Asphaltic Limestone Co.*, 1942, 315 U. S. 179; *Helvering* v. *Bashford*, 1938, 302 U. S. 454; *Minnesota Tea Co.* v. *Helvering*, 1938, 302 U. S. 609."

The Court of Appeals' citations of cases do not support its reasoning. *Gregory* v. *Helvering*, 293 U. S. 465, has nothing in common with the present case, as is clear from the opinion of Judge Learned Hand in *Chisholm* v. *Commissioner*, 79 F. (2d) 14. Judge Hand had written the opinion of the Court of Appeals in the *Gregory* case (69 F. (2d) 809), reversing the decision of the Board of Tax Appeals in favor of the taxpayer (27 B. T. A. 223), which it was the misfortune of the writer to be retained to support in the Court of Appeals and Supreme Court.

Presumably the Court of Appeals cited *Helvering* v. *Alabama Asphaltic Limestone Co.*, 315 U. S. 179, for the following dictum (p. 184):

> "Transitory phases of an arrangement frequently are disregarded under these sections of the revenue acts where they add nothing of substance to the completed affair. Gregory v. Helvering, 293 U. S. 465, 1355; Helvering v. Bashford, 302 U. S. 454. Here they were no more than intermediate procedural devices utilized to enable the new corporation to acquire all the assets of the old one pursuant to a single reorganization plan."

There the "transitory phases" were preliminary to the acquisition of ownership and the preservation of continuity of interest. Here the acquisition of ownership with the preservation of continuity of interest was not a preliminary transitory phase, but was accomplished by the issue solely of voting stock for all the properties of Riggs. The subsequent liquidation of Riggs was a mere addendum to the reorganization already consummated, and was free from tax under Section 112(b)(3) of the 1939 Code as an exchange of stock of the petitioner for stock of Riggs. See Section 111(c) and Section 115(c) of the 1939 Code (App. C, p.

28), expressly limiting recognition of gain to that determined under Section 112.

The *Alabama Limestone* case and *Helvering* v. *Bashford*, 302 U. S. 454, also cited by the Court were respectively decided for and against the taxpayer because in the former there was continuity of interest and in the latter there was not.

In *Minnesota Tea Company* v. *Helvering*, 302 U. S. 609, also cited by the Court, the taxpayer, following an exchange of its entire assets for cash and stock in another corporation, had distributed the cash to its stockholders who agreed to pay therefrom all the debts of the corporation. To the extent of such indebtedness the taxpayer corporation was not relieved of tax thereon since the stockholders did not receive such amount as their property.

The application to the present case seems remote, since the petitioner here could not under the laws of Delaware have acquired all of the assets of Riggs, except by statutory merger or by the procedure of issuing its stock therefor as was actually done. The mere liquidation of Riggs could not possibly have resulted in the petitioner receiving all the Riggs assets.

The opinion below animadverts on the petitioner's second point as a "belabored effort." Since counsel realized that the Tax Court, at the instance of the Government, might disregard what the petitioner actually did, in order to achieve tax liability on the theory of treating the final step of liquidation as the controlling event, it was believed that consideration might be given to the equities of the situation in disregard of a minute technical defect. This hope was blasted, but on the principle, as stated by Judge Harron, that "Petitioner is bound by what in fact was done" (R., p. 46). So far the Government has not been bound by what in fact was done in the reorganization.

To the petitioner, the Court of Appeals, to borrow the expression, seems to belabor the facts in order to uphold the Tax Court decision. In no other case that we know of has the liquidation of the corporation whose assets were acquired in a reorganization been regarded as of prime importance, overshadowing the actual transfer of its assets to the acquiring corporation. If the liquidation had not occurred, there would unquestionably have been a tax-free reorganization. The surrender of the stock of the acquired corporation, in exchange for the stock of the aequiring corporation received for the assets of the acquired corporation, has been a usual incident of a reorganization (Sec. 112 (b)(3), *supra*, p. 3), but never regarded as the predominant factor, converting a true reorganization into a mere liquidation.

The object of the reorganization, of course, was not to liquidate the Riggs business, but to merge it with the petitioner's. The dissolution of Riggs was merely incidental to the achievement of that object. The cases cited contain absolutely nothing to impair the petitioner's position in this case, but rather they support it. There was no "attempt to thwart taxation"; but on the contrary the lower courts have perverted the language and intent of the statute to impose a dishonest tax where none was intended.

If the lower courts' misconstruction of the statute involved only transactions under the Revenue Code of 1939, this Court might regard the plight of the present petitioner and others in the same position as not justifying review, but the same situation exists under the Internal Revenue Code of 1954, the pertinent provisions of which follow:

Section 368(a)(1) provides:

"(a) REORGANIZATION.—

(1) IN GENERAL.—For purposes of parts I and II and this part, the term 'reorganization' means—

(A) a statutory merger or consolidation;

(B) the acquisition by one corporation, in exchange solely for all or a part of its voting stock, of stock of another corporation if, immediately after the acquisition, the acquiring corporation has control of such other corporation (whether or not such acquiring corporation had control immediately before the acquisition);

(C) the acquisition by one corporation, in exchange solely for all or a part of its voting stock (or in exchange solely for all or a part of the voting stock of a corporation which is in control of the acquiring corporation), of substantially all of the properties of another corporation, but in determining whether the exchange is solely for stock the assumption by the acquiring corporation of a liability of the other, or the fact that property acquired is subject to a liability, shall be disregarded; * * *"

It will be noted that in the case of a "B" reorganization the previous ownership of stock in the acquired corporation is taken into account, but evidently existing ownership of stock of the acquired corporation by the acquiring corporation was deemed immaterial in the case of a "C" reorganization.

Section 361(a) provides:

"(a) GENERAL RULE.—No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization."

Section 354(a)(1) provides:

"(a) GENERAL RULE.—

(1) IN GENERAL.—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization. * * *"

These provisions, as well as those of the 1939 Code, were complied with by Riggs exchanging all its property solely for stock of the petitioner and by the exchange of the petitioner's Riggs stock for some of its own stock, in common with the other stockholders of Riggs, upon the dissolution of Riggs.

The history of Section 112(b)(6) shows that its passage was not intended in any way to curtail the scope of the reorganization provisions, but to permit a parent corporation by mere liquidation to take over assets of a subsidiary without recognition of gain or loss at the basis to the parent of its cost of the subsidiary's stock (R. A. 1935, Sec. 110). It had been urged that it was unfair, in the case of a corporation desiring to liquidate a subsidiary, to deprive the parent of the benefit of the cost basis it had for the subsidiary's stock when greater than the value of the subsidiary's assets. However, by the Revenue Act of 1936, because of the hardship which would result from the application of Section 112(b)(6) upon the liquidation of a prosperous subsidiary in which the parent had made only a small investment, the statute was amended to provide that the basis of the distributed property to the parent should be the basis to the subsidiary (1939 Code, Section 113(a)(15)). (By the 1954 Code, Section 334, alternative bases were prescribed in liberalization of the statute.)

The Court of Appeals here has rendered a decision essentially in conflict with a decision in the 8th Circuit in a similar case. In *Winston Bros. Co.* v. *Commissioner*, 76 F. (2d) 381 (C. C. A. 8, 1935), a parent corporation, which owned 68 per cent of the stock of a subsidiary, issued its stock for all the assets of the subsidiary, and the subsidiary was thereupon liquidated. The transactions were held to constitute a nontaxable reorganization. Although the *Winston Bros.* case was decided under pre-1934 law, petitioner believes that the addition of the requirement in the Revenue Act of 1934 that the exchange be solely for voting stock has not changed the force and effect of that decision.

Originally the Commissioner of Internal Revenue did not acquiesce in the Tax Court decision in the *Winston Bros.* case. In 1940, however, he reversed his non-acquiescence (1940-2 C. B. 8). Then in 1954, almost four years after the reorganization in question here, transactions such as the present were ruled to be taxable and the rule of the *Winston Bros.* case was limited to pre-1934 transactions (Rev. Rul. 54-396, 1954-2 C. B. 147). Still more recently the Internal Revenue Service has somewhat relaxed the 1954 ruling in Rev. Rul. 57-278, 1957-1 C. B. 124.

Here, as in *Winston*, the petitioner issued stock for assets, except that its stock so issued was solely voting stock, and then, as in *Winston*, on dissolution of the acquired corporation it received some of its own stock in exchange for its stock in the acquired corporation. See also *Fisher* v. *Commissioner*, 34 B. T. A. 1215, aff. 108 F. (2d) 707, cert. denied 310 U. S. 627; *Gutbro Holding Co.* v. *Commissioner*, 138 F. (2d) 16; *Peck & Peck* v. *Commissioner*, 42 B. T. A. 651 (1940); *Helvering* v. *Schoellkopf*, 100 F. (2d) 415; *Zenz* v. *Quinlivan*, 213 F. (2d) 914. Cf. *Transport Products Corp.* v. *Commissioner*, 25 T. C. 853, 858 (1956).

In short, the petitioner for purely business reasons wanted to combine the Riggs business with its own. It could do so (1) under the merger statutes of New York and Delaware, or (2) by issuing solely voting stock for the assets of Riggs and then dissolving it, or (3) by acquiring a few more shares of Riggs and then liquidating it. The petitioner chose the second method as more simple than the first and more in keeping with its aim of continuing the Riggs business than the third method. Naturally the petitioner preferred a non-taxable method, as all three methods were. Accordingly, under a reorganization plan the petitioner issued solely voting stock for all the assets of Riggs, pursuant to Section 112(g)(1)(C) and (b)(4) of the 1939 Code, and upon the dissolution of Riggs, pursuant to Section 112(b)(3) of the 1939 Code, exchanged its stock in Riggs, as did all the other Riggs stockholders, for the stock which it had issued for the Riggs assets. The course of the petitioner was in strict compliance with the language and intent of the Code provisions and with the Treasury regulations, Section 39.112(g)-(1) of Regulations 118 providing in part:

> "The purpose of the reorganization provisions of the Internal Revenue Code is to except from the general rule certain specifically described exchanges incident to such readjustment of corporate structures, made in one of the particular ways specified in the Code, as are required by business exigencies, and which effect only a readjustment of continuing interests in property under modified corporate forms. Requisite to a reorganization under the Code are a continuity of the business enterprise under the modified corporate form, and a continuity of interest therein on the part of those persons who were the owners of the enterprise prior to the reorganization. * * *"

The last portion of Section 112(b)(6) of the 1939 Code (and of the corresponding Section 332(b) of the 1954 Code) makes clear that the prior ownership by the acquiring corporation of even 80 per cent, or more of the stock of the acquired corporation does not preclude resort to the exchange provisions in Section 112(b)(3) and (4). It reads:

> "* * * for the purposes of this paragraph a transfer of property of such other corporation to the taxpayer shall not be considered as not constituting a distribution (or one of a series of distributions) in complete cancellation or redemption of all the stock of such other corporation, merely because the carrying out of the plan involves (i) the transfer under the plan to the taxpayer by such other corporation of property, not attributable to shares owned by the taxpayer, upon an exchange described in paragraph (4) of this subsection, and (ii) the complete cancellation or redemption under the plan, as a result of exchanges described in paragraph (3) of this subsection, of the shares not owned by the taxpayer."

So, an exchange of property of the acquired corporation for stock of the acquiring corporation is recognized as falling within paragraph (4) of Section 112(b), and the exchange of shares of the acquired corporation not owned by the acquiring corporation for shares of its stock is also recognized as falling within paragraph (3), both paragraphs dealing with exchanges pursuant to a tax-free reorganization.

There is not the slightest excuse for concluding that the enactment of Sec. 112(b)(6) was intended to curtail the scope of the reorganization provisions. That provision was originally intended to allow a corporation holding 80 per cent. of the stock of a subsidiary the basis of the parent's cost of the subsidiary's stock on a mere liquidation of the

subsidiary, but it was found that in most cases the subsidiary's basis for its assets exceeded the parent's cost and the statute was amended to allow the parent the benefit of the subsidiary's basis, which conformed with the rule applicable to reorganizations (1939 Code, Sec. 113(a)(15)).

The respondent's view would result in rendering impossible a non-taxable reorganization (except by statutory merger or consolidation) in all cases other than those in which the merging corporation held none of the stock or more than 80 per cent. of the stock of the merged corporation. What possible reason in sense or justice could there be for such a differentiation?

CONCLUSION

In conclusion, petitioner submits that a writ of certiorari should be granted because:

1. The decision of the Court of Appeals is in error with respect to the history and interpretation of the statute in question and in its misapplication of fundamental principles of tax law applied in decisions of this Court.

2. The Court of Appeals has decided an important question of federal tax law in conflict with a decision rendered by another Court of Appeals, which question has not been, but should be, settled by this Court.

3. The decision of the Court of Appeals creates substantial and unnecessary confusion in an area of interest to the entire business community, both under the Internal Revenue Code of 1954 and the Internal Revenue Code of 1939.

The petitioner has been the victim of vacillating treasury opinion, afterthoughts retroactively applied, and inconsistencies in the administration of the tax law.

Respectfully submitted,

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August , 1959

APPENDIX A

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the nineteenth day of May, one thousand nine hundred and fifty-nine.

Present:

HON. HAROLD R. MEDINA,
HON. CARROLL C. HINCKS,
Circuit Judges.

HON. WILLIAM C. MATHES,
District Judge.

BAUSCH & LOMB OPTICAL COMPANY,
Petitioner.

—v.—

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Appeals from The Tax Court of the United States

This cause came on to be heard on the transcript of record from The Tax Court of the United States, and was argued by counsel. ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said The Tax Court of the United States be and it hereby is affirmed.

A. DANIEL FUSARO,
Clerk.

APPENDIX B

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 239—October Term, 1958.

(Argued March 6, 1959 Decided May 19, 1959.)

Docket No. 25424

BAUSCH & LOMB OPTICAL COMPANY,

Petitioner,

—v.—

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Before:

MEDINA and HINCKS, *Circuit Judges*, and MATHES, *District Judge.**

On petition to review a decision of the Tax Court of the United States, Marion J. Harron, *Judge*.

Petitioner's claim that certain transactions in 1950 with Riggs Optical Company, of the voting stock of which petitioner owned 79.9488%, constituted a reorganization under either Section 112(g)(1)(C) or Section 112(g)(1)(A) of the 1939 Internal Revenue Code, and hence were tax free, was rejected. The Tax Court also rejected the contention

* United States District Judge for the Southern District of California, sitting by designation.

that there was a liquidation under Section 112(b)(6)(A). Reported at 30 T. C. 602. Affirmed.

HUGH SATTERLEE, Rochester, New York (Scott Stewart, Jr. and Thomas C. Taylor, Rochester, New York, on the brief), *for petitioner.*

MORTON K. ROTHSCHILD, Attorney, Department of Justice, Washington, D. C. (Charles K. Rice, Assistant Attorney General, Lee A. Jackson, Harry Baum and Melvin L. Lebow, Attorneys, Department of Justice, Washington, D. C., on the brief), *for respondent.*

MEDINA, *Circuit Judge*:

Petitioner Bausch & Lomb Optical Company, a New York corporation engaged in the manufacture and sale of ophthalmic products, on March 1, 1950 owned 9,923¼ shares of the stock of its subsidiary Riggs Optical Company, or 79.9488% of the 12,412 outstanding shares of Riggs. In order to effectuate certain operating economies, Bausch & Lomb decided to amalgamate Riggs with itself. To this end on April 22, 1950 Bausch & Lomb exchanged 105,508 shares of its unissued voting stock for all of the Riggs assets. An additional 433 shares of Bausch & Lomb stock went to 12 Riggs' employees.

On May 2, 1950, according to a pre-arranged plan, Riggs dissolved itself, distributing its only asset, Bausch & Lomb stock, pro rata to its shareholders. Bausch & Lomb thus received back 84,347 of its own shares which became treasury stock, while 21,161 shares went to the Riggs minority shareholders.

The Commissioner determined that the substance of these transactions was that Bausch & Lomb received the

Riggs assets partly in exchange for its Riggs stock and partly for its own stock, and that the gain which Bausch & Lomb realized upon the Riggs "liquidation" was subject to tax. In other words, that Bausch & Lomb parted with 21,161 shares of its own voting stock, plus 9,923¼ shares of its Riggs stock, for the transfer to it of all of the Riggs assets. Bausch & Lomb contends, however, that a "reorganization" was effected under Section 112(g)(1)(C) of the 1939 Internal Revenue Code,[1] and that it is therefore entitled to tax-free treatment.[2] The Tax Court sustained the Commissioner's position and held that the acquisition of the Riggs assets and the dissolution of Riggs must be viewed together, and that the surrender by Bausch & Lomb of its Riggs stock was additional consideration. The Tax Court accordingly held that the Riggs assets were not obtained "solely for all or a part of its voting stock." We agree.

Bausch & Lomb concedes that to qualify as a "C" reorganization, it could not furnish any additional consideration over and above its own stock. *Helvering* v. *Southwest Consolidated Corp.*, 1942, 315 U. S. 194; *Adwood Corp.* v.

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[1] Section 112(g)(1)(C) provides:

"(1) The term 'reorganization' means • • •

"(C) the acquisition by one corporation, in exchange solely for all or a part of its voting stock, of substantially all the properties of another corporation, but in determining whether the exchange is solely for voting stock the assumption by the acquiring corporation of a liability of the other, or the fact that property acquired is subject to a liability, shall be disregarded, • • •"

[2] Section 112(b)(3) provides:

"(b) *Exchanges Solely in Kind.*

• • •

"(3) *Stock for stock on reorganization.*—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization."

Commissioner, 6 Cir., 1952, 200 F. 2d 552, cert. denied, 346 U. S. 818; *Stoddard v. Commissioner*, 2 Cir., 1944, 141 F. 2d 76. Moreover, Bausch & Lomb admits, as the correspondence and minutes of pertinent meetings plainly show, that the acquisition of the Riggs assets and the dissolution of Riggs were both part of the same plan. Nevertheless, Bausch & Lomb asserts that the exchange of the Riggs assets for its stock should be treated as separate and distinct from the dissolution. The argument runs to the effect that, if the two steps are viewed apart from one another, a "C" reorganization is effected.

Petitioner contends that, even if a qualification according to the literal terms of Section 112(g)(1)(C) is not found, the amalgamation was in substance a "reorganization" because it has the attributes of one, including "continuity of interest" and business purpose. This is factually not quite true for, while the amalgamation may have been for genuine business reasons, the division into two steps served only to facilitate the liquidation of Riggs. It was considered easier to distribute Bausch & Lomb stock than distribute the Riggs assets. Hence the "business purpose" of dividing the liquidation into two steps lends no support to Bausch & Lomb's contention that in substance and actuality a reorganization was achieved. Moreover, the Congress has defined in Section 112(g)(1)(C) how a reorganization thereunder may be effected, and the only question for us to decide, on this phase of the case, is whether the necessary requirements have been truly fulfilled. It is for the Congress and not for us to say whether some other alleged equivalent set of facts should receive the same tax free status.

Nor does the fact that Bausch & Lomb may well have desired to hold the 84,347 shares of its own voting shares as treasury stock change our opinion of the transaction as a whole.

Bausch & Lomb suggests that under our present holding even if it had but a 1% interest in Riggs, the requirement that the acquisition be "solely for * * * its voting stock" could defeat Section 112(g)(1)(C) reorganization treatment. This hypothesis is a far cry from the facts disclosed in this record, and the lack of controlling interest surrounds it with a mist of unreality. In any event, it will be time to consider such a situation in all its aspects when, as and if it comes before us. We merely hold that the attempt to thwart taxation in this case by carrying out the liquidation process in two steps instead of one fell short of meeting the requirements of a "C" reorganization. See *Gregory* v. *Helvering*, 1935, 293 U. S. 465; *Helvering* v. *Alabama Asphaltic Limestone Co.*, 1942, 315 U. S. 179; *Helvering* v. *Bashford*, 1938, 302 U. S. 454; *Minnesota Tea Co.* v. *Helvering*, 1938, 302 U. S. 609.

Of course, the fact that Bausch & Lomb "could have" merged with Riggs and hence qualified the transaction as a reorganization under Section 112(g)(1)(A) is beside the point. For reasons of its own it chose not to do so. This is clearly not an "A" reorganization.

Bausch & Lomb also claims that a tax-free liquidation was effected under Section 112(b)(6)(A),[3] although it plainly lacked the necessary 80% of the voting stock. This belabored effort to claim ownership of the 51 shares of Riggs voting stock for which 12 of Riggs' employees had received credit on Riggs' books, so as to raise Bausch & Lomb's interest slightly above the 80% required by Section 112(b)(6)(A) has nothing whatever to commend it. As found by the Tax Court, Bausch & Lomb never was the legal or equitable owner of these shares, there was never any agreement on the part of the employees to assign them to Bausch & Lomb, and the original stock purchase agreements of the Riggs employees provided that if Riggs should be reorganized and its business acquired by another cor-

poration, a successor corporation would have the right to assume the contract and substitute its stock in the place of the Riggs' stock originally reserved under the stock purchase agreements. New arrangements were made later, in line with the provision of the original stock purchase agreements just referred to, and the employees received certain cash payments and the 433 shares of Bausch & Lomb stock mentioned in the opening part of this opinion. We find in the facts of this case no foundation whatever for the claim that a liquidation was effected under Section 112(b)(6)(A).

Affirmed.

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[1] Section 112(b)(6)(A) of the 1939 Code provides:

"(6) *Property Received by Corporation on Complete Liquidation of Another*—No gain or loss shall be recognized upon the receipt by a corporation of property distributed in complete liquidation of another corporation. For purposes of this paragraph a distribution shall be considered to be in complete liquidation only if

"(A) the corporation receiving such property was, on the date of the adoption of the plan of liquidation, and has continued to be at all times until the receipt of the property, the owner of stock (in such other corporation) possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and the owner of at least 80 per centum of the total number of shares of all other classes of stock (excepting nonvoting stock which is limited and preferred as to dividends), and was at no time on or after the date of the adoption of the plan of liquidation and until the receipt of the property the owner of a greater percentage of any class of stock than the percentage of such class owned at the time of the receipt of the property; • • •"

APPENDIX C

INTERNAL REVENUE CODE OF 1939

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) *Computation of Gain or Loss.*—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113(b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

* * * * * *

(c) *Recognition of Gain or Loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this chapter, shall be determined under the provisions of section 112.

* * * * *

(26 U. S. C. 1952 ed., Sec. 111.)

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

* * * * *

(c) [As amended by Sec. 147, Revenue Act of 1942, c. 619, 56 Stat. 798] *Distributions in Liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. * * *

(26 U. S. C. 1952 ed., Sec. 115.)

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No. 289

In the Supreme Court of the United States

OCTOBER TERM, 1959

BAUSCH & LOMB OPTICAL COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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CHARLES K. RICE,
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MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Bausch & Lomb Optical Company, the taxpayer, owned 79.95% of the stock of Riggs Optical Company. In 1950, pursuant to plan, Riggs transferred all its assets to Bausch & Lomb in exchange for 105,508 shares of Bausch & Lomb voting stock which it then distributed in liquidation to its stockholders, Bausch & Lomb receiving, upon surrending its Riggs stock for cancellation, 84,347 of the shares and the minority Riggs stockholders receiving the remaining 21,161. The sole issue here is whether those transactions resulted in a tax-free reorganization within the meaning of § 112(g)(1)(C) of the Internal Revenue Code of 1939 (26 U.S.C., 1952 ed.), which defines a "reorganization" as including "the acquisition by one

corporation, in exchange solely for all or a part of its voting stock, of substantially all the properties of another corporation."

The Commissioner, the Tax Court, and the court of appeals all held that, viewing the several steps as one, Bausch & Lomb had in effect acquired 79.95% of Riggs' assets in exchange for the surrender of its Riggs stock and only the balance in exchange for the 21,161 shares of its own stock that were not returned to it. Since the Riggs assets were thus not acquired *solely* in exchange for Bausch & Lomb voting stock, it followed that there was no reorganization under § 112(g)(1)(C) and that Bausch & Lomb was taxable on the capital gain measured by the excess of 79.95% of the value of the Riggs assets over its basis for the Riggs stock.

The decision below is clearly correct. Although the single step of the exchange of Riggs assets for 105,508 shares of Bausch & Lomb stock literally meets the § 112(g)(1)(C) definition, it is settled that the several steps of an integrated plan must be viewed together.[1] If the steps are combined here, it is apparent that the consideration given by Bausch & Lomb for the Riggs assets was not 105,508 shares of its stock but only 21,161 of those shares (84,347 shares being returned to it) plus the surrender of the Riggs stock that Bausch & Lomb had previously acquired.

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[1] *E.g., Helvering* v. *Southwest Corp.*, 315 U.S. 194, 200; *Helvering* v. *Bashford*, 302 U.S. 454, 458; *Minnesota Tea Co.* v. *Helvering*, 302 U.S. 609; *Gregory* v. *Helvering*, 293 U.S. 465; *Georgia-Pacific Corp.* v. *United States*, 264 F. 2d 161, 166 (C.A. 5); *Morgan* v. *Helvering*, 117 F. 2d 334 (C.A. 2); *Barker* v. *United States*, 200 F. 2d 223, 231 (C.A. 9).

presumably for cash or other property. "'Solely' leaves no leeway. Voting stock plus some other consideration does not meet the statutory requirement." *Helvering* v. *Southwest Corp.*, 315 U.S. 194, 198. The fact that part of the consideration given was other than Bausch & Lomb voting stock thus prevents the transaction from qualifying under § 112(g)(1)(C).

There is no conflict[2] or any other reason for review of the question by this Court. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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SEPTEMBER 1959.

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[2] Petitioner's assertion of a conflict with *Helvering* v. *Winston Bros. Co.*, 76 F. 2d 381 (C.A. 8), is answered by its own admission (Pet. 15) that the Revenue Act of 1928 there construed (45 Stat. 791) did not contain the solely-for-voting-stock requirement, which was first added by the Revenue Act of 1934 (48 Stat. 680). That transactions qualifying as reorganizations under the one may not qualify under the other is clear. See *Helvering* v. *Southwest Corp.*, 315 U.S. 194, 198-199, and compare the companion case, *Helvering* v. *Limestone Co.*, 315 U.S. 179.

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REPLY MEMORANDUM TO RESPONDENT'S MEMORANDUM IN OPPOSITION

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REPLY MEMORANDUM TO RESPONDENT'S MEMORANDUM IN OPPOSITION

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REPLY MEMORANDUM TO RESPONDENT'S MEMORANDUM IN OPPOSITION

Respondent's Memorandum in Opposition is brief, and its brevity appears to make simple an intricate problem of tax law.

It is stated that "There is no conflict or any other reason for review: . . ."

Whether there is a conflict between the Courts of Appeal depends upon the meaning of the word "solely" in the statutory definition of reorganization. Neither of the opinions below in this case reviews or discusses the reasons for the enactment of "solely" into tax law. "Solely" represents the statutory enactment of the judicially imposed continuity of interest requirement, and it was inserted to prevent sales from qualifying as tax free reorganizations. Thus,

where a disguised sale is involved, no leeway is or should be permitted. But where, as here, there is unquestioned continuity of interest and no sale is involved, "solely" should not be stretched in a way which not only thwarts the clearly defined intent of Congress but also does not further any policy of tax administration. Such an unwarranted interpretation of "solely" taxes the bona fide joining of two related corporations when the very same transaction between two unrelated corporations would be nontaxable.

If "solely" is interpreted as legislative history and prior decisions indicate it should be, then there is a conflict. It is the novel interpretation of "solely" reflected in the decisions of the Tax Court and the Court of Appeals here, going beyond any decision of this or any other court, which is the very question at issue in this case. It is appealing but meaningless to resolve the conflict by saying that there is no conflict.

Respondent's Memorandum in Opposition is also appealingly simple in its statement that "If the steps are combined here, it is apparent that" Bausch & Lomb did not give solely its voting stock for the Riggs properties. The step transaction principle has never been applied by this Court in this type of transaction, and its application by the Court of Appeals in this case where a mere change of business form is involved should be sufficient ground in itself for the granting of a writ. Furthermore, even if the principle is to be applied here, it is "apparent" that Bausch & Lomb did give solely its voting stock for the Riggs properties. The Riggs stock previously owned by Bausch & Lomb, which the Treasury feels defeats the reorganization, was not surrendered in exchange for any Riggs properties, but instead, if the two transactions are

one, was in effect changed into Bausch & Lomb treasury stock. To conclude, as would necessarily follow from the Treasury position, that the definition of "properties" in Section 112 (g) (1) (C) includes both the properties of Riggs before the reorganization and the Bausch & Lomb stock held by Riggs after the exchange of stock for the properties is a view that has no basis in statutory or case law and which ignores completely the existence of Section 112 (b) (3) and its importance in the reorganization of corporate interests.

There are, furthermore, other reasons for review. The petition states that the decision of the Court of Appeals for the Second Circuit creates substantial and unnecessary confusion in an area of interest to the entire business community. The leading article in "Taxes, The Tax Magazine" for March, 1959 entitled "How to Avoid Stumbling Blocks in Reorganizations" is based on (and criticizes) the Tax Court decision in this case. A more recent article in "Taxes, The Tax Magazine" for August, 1959, entitled "Tax Problems in Acquiring the Remaining Interest in a Partially Owned Corporation" finds the Court of Appeals decision in this case unjustified. It discusses the strained alternatives which practitioners must use on account of this case in order to avoid a taxable result when rearranging corporate interests in similar situations.

The program for the 18th Annual Institute on Federal Taxation sponsored by New York University to be held November 4-13, 1959 schedules a discussion of "The Bausch & Lomb Decision" as one of the "Current Problems in Taxable and Tax Free Reorganizations."

In short, the holding of the Court of Appeals presents an anomalous rule which has created considerable discus-

sion and confusion in the current tax law. The petition for a writ of certiorari should be granted.

Respectfully submitted,

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September 21, 1959